

August 4, 2016

Mr. Robert deV. Frierson  
Secretary  
Board of Governors of the Federal Reserve System  
20<sup>th</sup> St. and Constitution Ave. NW  
Washington, DC 20551

**Re: Docket No. R-1538 and RIN No. 7100 AE-52 – Restrictions on Qualified Financial Contracts of Systematically Important U.S. Banking Organizations and the U.S. Operations of Systemically Important Foreign Banking Organizations; Revisions to the Definition of Qualifying Master Netting Agreement and Related Definitions**

Dear Mr. Frierson:

On behalf of the National Association of Insurance Commissioners (NAIC)<sup>1</sup>, we write today regarding the Board of Governors of the Federal Reserve System's (Board) proposed rule on qualified financial contract (QFC) restrictions and the definition of qualifying master netting agreements. The NAIC respectfully submits the following comments to the Notice of Proposed Rulemaking and Request for Comment published in the May 11, 2016 issue of the Federal Register.

The proposed rule would amend several definitions in the Board's capital and liquidity rules to ensure the proposal would not have unintended effects for the treatment of covered entities' netting sets under those rules, including "qualifying master netting agreement," "collateral agreement," "eligible margin loan," and "repo-style transaction." Question 23 of the notice asks if it would be appropriate to incorporate state law resolution regimes into these definitions. The NAIC believes that the proposed definitions should include references to state resolution regimes (such as insurance receiverships), and encourages the Board to do so.

**Background and Related NAIC Activity**

As the primary regulators of insurance companies in the United States, state regulators are charged with protecting insurance company policyholders. In October, 2013, state regulators, through the NAIC, adopted a *Guideline for Stay on Termination of Netting Agreements and Qualified Financial Contracts* (#1556). This guideline encourages states to amend insurance receivership law to adopt a 24-hour stay

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<sup>1</sup> Founded in 1871, the NAIC is the U.S. standard-setting and regulatory support organization created and governed by the chief insurance regulators from the 50 states, the District of Columbia and the five U.S. territories. Through the NAIC, state insurance regulators establish standards and best practices, conduct peer review, and coordinate their regulatory oversight. NAIC members, together with the central resources of the NAIC, form the national system of state-based insurance regulation in the U.S.

provision, similar to those found in the federal bankruptcy code and the Federal Deposit Insurance Act (FDIA)<sup>2</sup>, which would prohibit the exercise of early termination rights under a QFC during the stay. As the immediate exercise of termination rights can cause a rapid dissipation of an insurer's assets, a stay can help to preserve the insurer's funds, and mitigate the impact of an insolvency on policyholders and other claimants.

### **Subsequent Federal Rules' Failure to Include State-Based Stays Raises Problems**

Subsequent to the NAIC's adoption of *Guideline #1556*, proposed and interim final rules from the Board and other federal financial regulators in 2014 and 2015 failed to include state-based stays in their definitions of "eligible master netting agreement."<sup>3</sup> These rules recognize stays from (i) the FDIA, (ii) Title II of the Dodd-Frank Act, (iii) similar laws applicable to government sponsored enterprises, and (iv) similar laws of foreign jurisdictions. However, the rules did not recognize stays found in state law. This non-recognition of state-based stays renders netting agreements entered into by insurance companies and counterparties in states with stay provisions ineligible for consideration under the final definition of "eligible master netting agreement."<sup>4</sup> This in turn has negative consequences for insurers subject to state-based stay provisions including higher collateral requirements and credit charges from counterparties.

At least one state that had enacted a 24-hour stay provision pursuant to the NAIC guideline has been forced to repeal or remove these provisions in order to avoid harm to its domestic insurance companies. Continued non-recognition of state-based stays in federal rules related to netting will also discourage additional states from enacting them. The absence of such stays also subjects the U.S. regulatory system to international criticism. The Financial Stability Board's *Key Attributes of Effective Resolution Regimes for Financial Institutions* (Key Attributes) envisions all jurisdictions having a temporary stay on termination of netting agreements and QFCs. (See Key Attribute 4.3 and Appendix I - Annex 5.) In its 2015 review of the Key Attributes for the U.S. banking and insurance sectors, the International Monetary Fund noted that *NAIC Guideline #1556* had been enacted "to a very limited extent" by the states.

### **Conclusion**

We encourage you to incorporate state law resolution regimes into all applicable federal rules related to QFC's, qualifying master netting agreements, and all related definitions. The objectives of the proposed rules support the inclusion of stays under state insurance insolvency laws. There is no rational basis for disregarding stays in U.S. insurance receivership proceedings, while recognizing stays in similar foreign proceedings. Further, insurance companies should not be penalized for states putting into place the same limited stay provisions that federal and international regulators acknowledge to be prudent for resolution. We believe updating the definitions in question to incorporate state law resolution regimes would encourage states to resume efforts to put the stays laid out in *NAIC Guideline #1566* into place, would put the insurance receivership regime on parity with other financial sector resolution regimes, and ensure U.S. insurers are on a level playing field with other financial market participants.

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<sup>2</sup> 12 U.S.C. § 1821(c)(9)-(12).

<sup>3</sup> See CFTC Proposed Rule at 79 FR 59898 (October 3, 2014); OCC and Board Interim Final Rule at 79 FR 78287 (December 30, 2014); FDIC Proposed Rule at 80 FR 5063 (January 30, 2015).

<sup>4</sup> Board, OCC, FDIC, FHFA, Farm Credit Administration Joint Final Rule at 80 FR 74840 (November 30, 2015).

Sincerely,



John M. Huff  
NAIC President  
Director  
Missouri Department of Insurance,  
Financial Institutions and Professional Registration



Theodore K. Nickel  
NAIC President-Elect  
Commissioner  
Wisconsin Department of Insurance



Julie Mix McPeak  
NAIC Vice President  
Commissioner  
Tennessee Department of Commerce and Insurance



Eric A. Cioppa  
NAIC Secretary-Treasurer  
Superintendent of Insurance  
State of Maine, Department of Professional and  
Financial Regulation, Bureau of Insurance